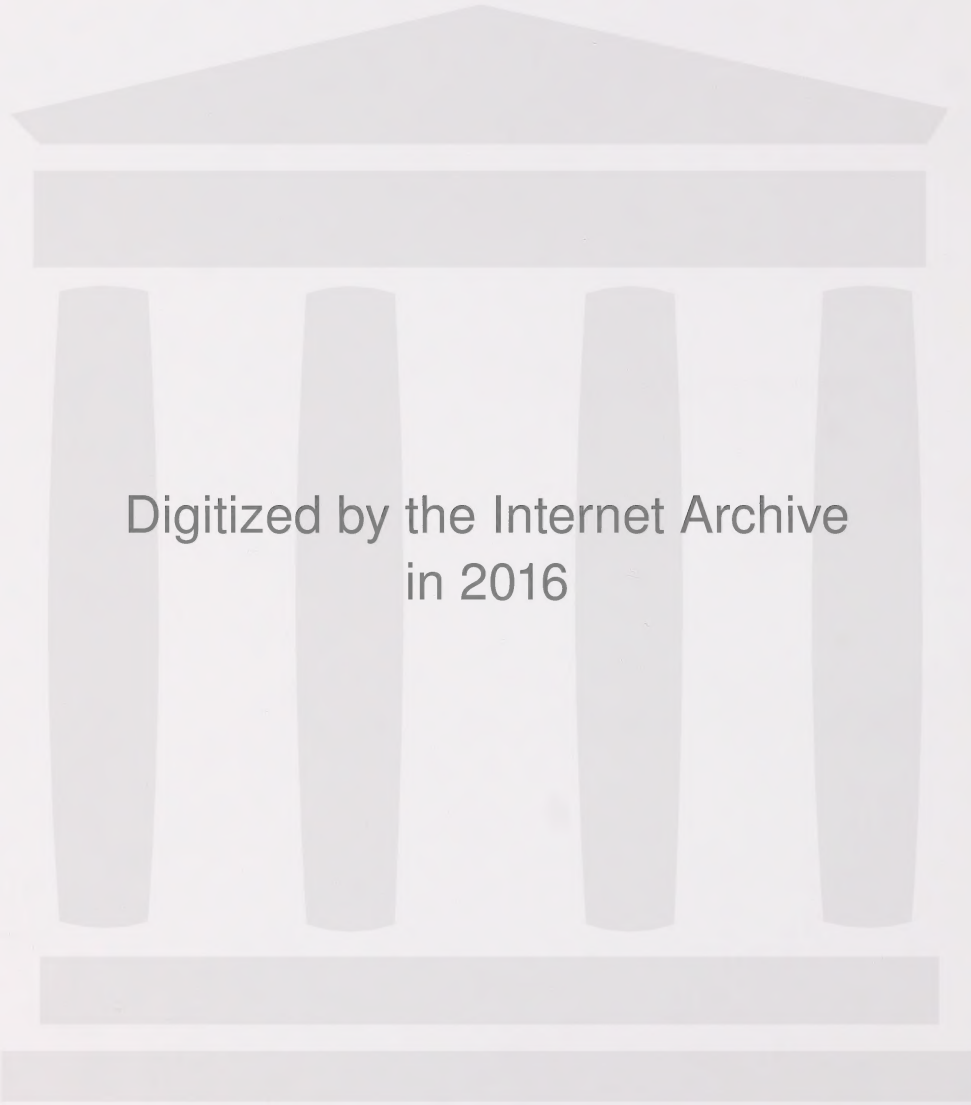


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ANNUAL REPORT 2005 - 2006



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OUR MISSION

We help customers fulfill their business goals
by offering unique financial services
in the development of business and agri-industry.

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BOARD OF DIRECTORS

Bob Splane, Chairman, Boyle
Brad Klak, Lacombe
Lynn Dechant, Fairview
Gene Dextrase, High Level
M. Barry Holmes, Rocky Mountain House
Wayne Wagner, Edmonton
H.D. (Harry) Haney*, Airdrie
Gail Surkan*, Red Deer
Joe Makowecki*, Edmonton
Barry Mehr, Edmonton
Gerard Oosterhuis, Bow Island

*was a Board member for a part of this year.

EXECUTIVE MANAGEMENT TEAM

Brad Klak, President and Managing Director
R. (Krish) Krishnaswamy, Vice-President, Finance
Merle Jacobson, Vice-President, Risk Management
Rick Bell, Vice-President, Lending
Donna Bryden, Senior Manager, Human Resources

...unique financial services to grow Alberta.

LETTER OF TRANSMITTAL

May 31, 2006

The Honourable Doug Horner
Minister of Agriculture, Food and Rural Development
229 Legislature Building
Edmonton, Alberta
T5K 2B6

Minister:

On behalf of the Board of Directors, we are pleased to submit the eleventh annual report of the Agriculture Financial Services Corporation.

As required by Section 15 of the *Agriculture Financial Services Act* (RSA 2000, c. A-12) the report contains a summary of the transactions and affairs of the Corporation, its revenues and the application of its expenditures for the fiscal year ended March 31, 2006. The report also contains audited financial statements, including a balance sheet, a statement of revenue, expense and surplus and a statement of cash flows.

Yours truly,

A handwritten signature in black ink, appearing to be 'Bob Splane', with a long horizontal line extending to the right.

Bob Splane
Chairman

A handwritten signature in black ink, appearing to be 'Brad Klak', with a stylized, cursive script.

Brad Klak
President and Managing Director

MINISTER'S MESSAGE



A YEAR AT A GLANCE...

My first year as Minister of Alberta Agriculture, Food & Rural Development (AAFRD) has been exciting and presented many opportunities and challenges.

I experienced firsthand the volatile nature of the farming industry and realized it can be ruthless if we are not prepared for the obstacles. It was reconfirmed to me the one constant in farming and rural community is change. Without change there can be no growth or diversity. It is with a sense of satisfaction that I have witnessed Alberta producers overcome hardships. The dream of continuing the family farm can be realized through innovative and entrepreneurial skills. It has been my privilege and honour to stand beside the resilient men and women who represent Alberta's agri-business today.

The competitive and courageous spirit of Alberta's producers and farmers, in the face of adversity has made agriculture the foundation of our economy. Even in the new millennium, agriculture continues to be a dynamic industry with an ever changing, ever challenging presence. Managing today's complex

farms and agri-businesses calls for determination and cutting edge strategies in our management practices.

THE CHALLENGES AND RESPONSES...

Border closures to live animal exports, new cases of bovine spongiform encephalopathy (BSE) and the lack of slaughter capacity continued to create stress for Alberta's beef industry. In response to these challenges, we concentrated our energy toward meeting the need to process more product in Alberta rather than exporting live animals.

AFSC aligned itself with a key objective of Alberta's six-point BSE recovery strategy. Our commitment to assist the meat processing industry by increasing slaughter capacities resulted in the construction or expansion of ten slaughter facilities and value-added food processing operations. We launched programs that financially supported investors of these projects and increased market opportunities for Alberta beef. The industry offered new value-added processing and new markets for specialty crops.

Low commodity prices, high input costs, lingering effects of drought and the rising Canadian dollar are having a devastating impact on our grains and oilseed sector. Many producers face financial crisis and cash flow problems. Statistical information indicates that grain, oilseed and pulse crop prices are at the lowest levels in the last ten years. This, coupled with rising input costs such as fuel, fertilizer and labour, which are determined outside the agriculture market, has exacerbated the financial crisis. The Alberta government undertook an initiative to advocate grain marketing reforms, including marketing choice for wheat and barley growers.

Under the CAIS Program, the Reference Margin Pilot Project was initiated to provide higher support levels which partially off-set the negative impact of drought and BSE in the past five years. We are committed to making CAIS predictable, simple, responsive, timely, and more bankable. Information sessions and input workshops were held across Alberta to help us gather information about our customers' needs.

Key strategies and initiatives for developing alternative uses for grains and oilseeds, such as bio-diesels, ethanol and bio-lubricants will help increase demand for commodities and meet the need for environmentally friendly products.

AFSC is to be commended for its leading role in introducing several enhancements to existing programs. Spring Price Endorsement (SPE) and Revenue Insurance Coverage (RIC) were made more affordable and the price risk protection was enhanced. These programs help counteract producers' vulnerability to unpredictable world commodity markets and soaring input costs. Our goal is to provide Alberta's producers with the best business risk management tools possible.

AFSC is moving towards having a one ministry approach where the government will provide the policy direction and AFSC will deliver agriculture services for the direct benefit of rural Albertans. Initiatives are being developed to avoid duplication whenever possible including a move towards a one window approach.

THE YEAR BEFORE US...

In the coming year there will be new challenges. Rather than cowering from transition, we want to be ready for it. We will be responsive and proactive in our programs and put in place the best risk management protection for Albertans.

The Alberta government is committed to working on short-term, as well as long-term recovery strategies for our grains and oilseeds sector. Early in 2006 we announced a three-point recovery framework that will

see better business risk management tools (including a revamping of CAIS), new crop uses, technologies and varieties, and enhanced business, investment and marketing tools. We are exploring what the government, in partnership with producers, can do to ensure this sector is forefront through innovation, new technologies and by taking advantage of new opportunities.

I feel a tremendous sense of pride in our employees who have worked hard to listen to our partners in agri-business and are committed to their success. Without actions, words are meaningless and we will strive to learn more and work hard at being leaders in providing reliable support mechanisms for our customers.

I am confident that the determination and resilient spirit of Alberta's farmers and business community, in partnership with dedicated service providers, will guarantee Alberta's agri-business success and prosperity for generations to come.



Doug Horner
Minister of Alberta Agriculture, Food and Rural Development



Photo courtesy of Lacombe Globe

CHAIRMAN'S MESSAGE

2005-06 was a year of change for AFSC, as well as for our producers. In June 2005 the Corporation proudly celebrated the Centennial year and the Grand Opening of the building extension to the Lacombe Central Office.

AFSC staff enjoyed the first staff conference in 12 years and were encouraged to focus on client service excellence. Under the direction of our new President and Managing Director, Brad Klak and a new management team, AFSC successfully transitioned through a difficult re-structuring of the Corporation. On behalf of the Board of Directors, I would like to thank the management team and all employees for effectively re-engineering the business processes to serve our customers better.

AFSC is committed to continuous improvement towards becoming an excellent customer service provider with relevant products and responsive delivery models that consistently exceed the expectations of our customers. In order to better serve our customers, the business processes were reviewed to direct resources and enhance support where needed, while cutting inefficiencies and duplication. The restructuring process focused on increasing our capacity to take on new growth, while maintaining excellent customer service.

The Board is thankful to Honourable Doug Horner, Minister of Alberta Agriculture, Food and Rural Development (AAFRD) for his wisdom and vision for rural Alberta, which continues to bring a refreshing perspective to the Corporation's strategic direction.

Our Corporate vision **to provide unique financial services to grow Alberta** has worked itself out through our goals. Our strategic priorities provided direction and set the course for the Corporation.

In order to be leaders in finding solutions that fit the changing needs of our customers, AFSC **reviewed the program expectations** and improved our customer's understanding of our products. The core programs were reviewed to ensure they were relevant and met the stakeholders and customers expectations. We explored ways to improve Insurance, Lending and the Canadian Agricultural Income Stabilization (CAIS) program and their delivery effectiveness.

AFSC is becoming a proactive catalyst, merging farm and commercial lending into one. Our evolving lending programs are targeted towards growth and to improving customer service. The new Alberta Farm Lending Program (AFLP) is designed to facilitate and simplify lending for farmers by blending existing farm lending programs, as well as clarifying program objectives and eligibility criteria.

It was exciting for our commercial and lending staff to be part of a number of success stories. AFSC provided financing to support investors in increasing slaughter capacity and expanding beef product and market development in Alberta. Since 2004, a number of projects for new and expanded slaughter facilities and value-added processing operations were approved. These projects will increase daily slaughter capacity.

We also approved new investment in 207 rural businesses and 93 new agri-businesses. Financing was provided for 899 farm lending projects totaling \$132 million.

Timothy Hay insurance was developed for the 2006 crop year. Production Insurance implemented satellite imagery and moisture deficiency insurance for pasture. More crops were added under silage and green feed.

We now have the right components in place to lead the way in partnership as hybrid lenders and risk managers, with both the Alberta government and AFSC working together on behalf of our agri-business partners.

AFSC further **improved customer service through the effective use of information technology** to deliver its products and services.

We implemented improvements to Production Insurance and CAIS and reviewed their delivery effectiveness. We began work on an adjuster automation pilot which will allow adjusters to complete field inspections on-line, reducing time, travel and paperwork. The simplified automatic renewal of Production Insurance will mean producers will no longer be required to visit the office to renew insurance contracts.

An e-business strategy is being developed which will provide clients and accountants easy on-line access to information about their CAIS applications and plans are in place to further enhance the system to enable on-line filing. A new CAIS claims system is



Photo courtesy of Lacombe Globe

in advanced stages of completion which will enable the Corporation to automate certain processes, resulting in a quicker turnaround on claim processing.

All 51 offices of AFSC located throughout Alberta are now connected by SuperNet, thus contributing to our efficiency. The Corporation has plans to leverage the SuperNet by providing new features such as video conferencing, better access to corporate systems, web-based communication channels and e-business in the future.

AFSC will focus on **effective succession planning, training and development of employees.**

We are committed to employee excellence and will provide the appropriate training and development opportunities for all staff. Our focus on customer service will be enhanced by ensuring our employees' success, providing them with the skills to better serve our clients, and by encouraging innovation in our program responses.

While AFSC is in the business of ensuring the success of producers, agri-business and commercial businesses, we realize that it is the people behind those businesses that we need to understand and support. Despite the growing complexity of farming and agri-business ventures in Alberta, our job has never been clearer. We need to work hard every day to help our customers achieve their financial hopes and dreams.

Bob Splane, Chairman

CORPORATE GOVERNANCE

As a provincial Crown Corporation, AFSC serves in a public policy role for the Government of Alberta. The Board of Directors provides leadership and direction to the Corporation and oversees management and performance.

MANDATE

The Board is responsible to the Minister of Alberta Agriculture, Food and Rural Development (AAFRD). The roles and responsibilities of the Board are set out in the Agriculture Financial Services Act and in a Memorandum of Understanding (MOU) between the Minister and the Board, which is updated annually. The MOU articulates the Board's responsibilities under the following major areas:

- Strategic Planning
- Enterprise Risk Management and Internal Controls
- Fiscal Responsibilities and Financial Reporting
- Communication with Stakeholders
- Establishing High standards of Integrity and Ethical Conduct

COMPOSITION OF THE BOARD

The Board consists of 11 directors. There are nine independent directors and two inside directors, namely the President and Managing Director of AFSC and the Deputy Minister of AAFRD. The Minister of AAFRD appoints all Board members. The Board members have varied skills and experience and are entrepreneurs, primary agricultural producers, and agribusiness owners/operators. The Board Chair and Committee Chairs are independent members. See page 1 for a complete list of Directors.

GOVERNANCE

The Board members adhere to the Board Governance Handbook. New Board members are provided orientation as soon as they assume their duties. The Board Code of Conduct and Ethics is reviewed annually, with each Board member annually confirming compliance. The Board, its Committees and individual Board members annually assess its performance through a structured process of self-

evaluation. With the assistance of an outside facilitator, yearly the Board identifies areas of potential development to enhance its effectiveness in governance and in pursuing strategies to achieve continuous improvement.

The Board meets monthly and Committees meet as often as required. The Board also regularly meets in-camera without management present. The Board ensures that public policy is considered in all decisions. Board members also participate in seminars and conferences to further enhance their skills in dealing with Corporate business issues and governance.

STEWARDSHIP

Strategic Planning:

The Board annually conducts a Strategic Planning retreat. At the retreat, the Board reviews and updates the Corporate Vision, Mission and Goals. They also review the progress made on the previous year's Strategic Plan and set Strategic Priorities for the coming year and beyond. In addition, the Board in its regular meetings reviews monthly reports from management on key activities of the Corporation under each of the Strategic Priorities.

Enterprise Risk Management and Internal Controls:

The Board and its Committees periodically review the Enterprise Risk Management document. This document identifies the major risks to which the Corporation may be exposed and ensures risk mitigation measures and internal controls are in place to make certain that the Corporation is adequately protected from identifiable risks.

Fiscal Responsibilities and Financial Reporting:

The Board, through its Audit Committee, ensures fiscal management by quarterly appraisal of forecasts and variances from budget. The Committee also reviews quarterly financial statements and key supporting schedules. The Committee examines Audit Plans of both the Internal Audit department and the Auditor General of Alberta to ensure prudent fiscal management and transparent financial reporting. The Board reviews and approves the annual financial statement and meets with the Auditor General without management present.

Communication with Stakeholders:

The Board periodically meets with organizations representing producers and businesses to obtain first-hand feedback on effectiveness of AFSC's products and services and discuss emerging issues. In addition, the Board tours the regions to meet with individual producers and businesses to understand their operations and challenges. These interactions help the Board to explore opportunities to enhance existing products and services and/or offer new products and services. On an Annual basis the entire Board meets with the Minister, while the Chair meets with the Minister and other stakeholders more often as required.

High Standards of Integrity and Ethical Conduct:

All new Board members are screened prior to appointment to ensure no potential conflict of interests exists. The Board members confirm compliance with the Code of Conduct and Ethics annually. The Code prescribes rules for dealing with situations where one or more Directors have private interest in any matter the Board considers for a decision.

BOARD COMMITTEES

For effective governance, the Board has established the following Committees to oversee certain functions. The Board approves the terms of reference, membership and reporting requirements of each Committee. To ensure independence, the Audit Committee and Hearings Committee are composed only of outside directors.

Governance Committee:

Reviews and makes recommendations to the Board with respect to governance practices, updates Board Governance manual, committee structure and memberships, Enterprise Risk Management and the MOU with the Minister.

Audit Committee:

Reviews quarterly forecasts and financial statements, internal and external audit plans and reports and Enterprise Risk Management relating to these areas.

Credit Committee:

Reviews new and modified Lending products, services and policies, approves loans and guarantees that exceed prescribed limits, reviews loan portfolio structure and performance.

Hearings Committee:

Handles the appeal and review processes, conducts appeals/reviews and reports results to the Board.

DIRECTOR	BOARD MEETINGS ATTENDED	COMMITTEE MEETINGS ATTENDED
DECHANT, LYNN	17 OF 19	10 OF 11
DEXTRASE, GENE	18 OF 19	13 OF 15
FALKENBERG, AARON*	3 OF 3	5 OF 5
FROELICH, ART*	7 OF 8	4 OF 6
HANEY, HARRY*	10 OF 11	7 OF 7
HOLMES, BARRY	16 OF 19	16 OF 16
KLAK, BRAD	19 OF 19	17 OF 17
KOTELKO, BERN*	8 OF 8	8 OF 8
MAKOWECKI, JOE*	11 OF 11	7 OF 7
MEHR, BARRY	17 OF 19	N/A
OOSTERHUIS, GERARD	17 OF 19	10 OF 11
SPLANE, BOB	19 OF 19	17 OF 17
SURKAN, GAIL*	15 OF 15	4 OF 4
WAGNER, WAYNE	19 OF 19	24 OF 25
*was a Board member for part of this year.		

BOARD COMMITTEE MEMBERSHIP

GOVERNANCE COMMITTEE

Chair: Gail Surkan
Bob Splane
Gene Dextrase
Wayne Wagner
Brad Klak
Barry Holmes

CREDIT COMMITTEE

Chair: Wayne Wagner
Joe Makowecki
Harry Haney
Bob Splane
Brad Klak

AUDIT COMMITTEE

Chair: Barry Holmes
Lynn Dechant
Gene Dextrase
Gerard Oosterhuis
Wayne Wagner

HEARING COMMITTEE

Chair: Gene Dextrase
Lynn Dechant
Joe Makowecki
Gail Surkan
Barry Holmes
Harry Haney
Gerard Oosterhuis

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL HIGHLIGHTS

The following information should be read in conjunction with AFSC's financial statements and attached notes.

2005-06 has been yet another successful year of operations for AFSC. The Corporation recorded a surplus of \$175.6 million, mainly due to crop losses being less than premium revenues.

Revenue for 2005-06 increased marginally from the previous year due to a higher contribution from the Province of Alberta to fund more claim payments under the CAIS Program, as a result of changes to the calculations of support levels for the 2003 to 2005 claim years.

Corporate expenses in 2005-06 decreased from the previous year, mainly as a result of lower indemnities.

The loan portfolio decreased by \$4 million, largely due to loan repayments being higher than loan disbursements. The allowance for doubtful accounts was decreased to 3.78% of the total loan portfolio from 4.28% in the previous year. This is reflective of some recovery from the impact of the BSE crisis, and steady land prices in the province.

RISK MANAGEMENT

The business activities of AFSC involve risks. A comprehensive Enterprise Risk Management plan and practices help us to manage our risks.

The Board and its Committees are responsible for reviewing management's Enterprise Risk Management plan and practices, including ensuring systems and internal controls are in place to mitigate identified risks to acceptable levels. The management, at all levels are responsible for the ongoing monitoring of risks and putting in place appropriate measures to manage them. The following discussion identifies some of the key risks the Corporation faces and how the risks are mitigated.

CREDIT RISK

Credit risk is the possibility that a debtor will not pay amounts owing to AFSC, thus resulting in a loss. To mitigate this risk, AFSC has developed the following policies.

The lending portfolio encompasses our largest credit risk. Lending staff monitor loan accounts

continually to ensure prompt response to any difficulties customers may encounter. Security requirements are contingent on the risk involved in each individual operation. For example, higher security levels would be required for enterprises needing specialized or customized equipment, or those involved with new and emerging businesses, than would be required for more established businesses. The above policies do not eliminate risk, but they do reduce the risk of significant losses.

The Corporation invests surplus funds generated by production and hail insurance operations. To mitigate the risk of potential non-realization of investment, the Corporation invests only in securities with the Government of Canada or any Canadian provincial governments and/or corporations that have superior credit quality and offer secured investments.

A portion of payments under the CAIS program has resulted in overpayments to participants with a risk of potential non-repayment of the overpayments. This risk is mitigated by providing a rebate for repayments within 90 days from notification of overpayment and to convert overpayments to an interest bearing loan with a repayment period of up to 10 years. The Corporation also has a right of offset against payments under CAIS and other programs such as Production Insurance. Where the Corporation is not able to recover overpayments from future program payments, the Corporation is committed to recovering the overpayment by pursuing collection through other means.

The Corporation provides insurance coverage on crops, effective at the signing of a contract of insurance, with or without payment of premiums in full. Non-collection of outstanding insurance premiums is a risk. To minimize this risk, a discount is provided for early payment of insurance premiums, and payment arrangements are set for all customers not taking advantage of the offered discount. Insurance staff closely monitor outstanding premiums, and collection action is taken promptly when required. Insurance contracts are not allowed to be renewed for future years if premiums for the prior year are outstanding at the time of renewal of insurance contracts.

To mitigate credit risk relating to non-recoverability of reinsurance proceeds from private reinsurance companies, AFSC – through its reinsurance broker – monitors the concentration of credit risk for the insurance contract it holds with each reinsurer and

evaluates the financial position of each reinsurer. There is no significant reliance on any one reinsurer.

INTEREST RATE RISK

Interest rate risk is the impact future changes in interest rates have on cash flows and fair value of assets and liabilities.

To mitigate this risk, AFSC matches the repayment timing of amounts borrowed with the repayment timing of loans made as closely as is practical. At March 31, 2006, the gap between the amount of loan and debt repayments due for periods of one to five years and six to ten years is reasonable. The debt due over ten years is about \$56.2 million lower than the estimated loan repayments during the same period because the loans due over a period of more than ten years are funded partly by the accumulated surplus from lending operations of \$71.5 million. Overall, the gap and consequent risk is low. AFSC's Investment Policy of surplus funds related to production and hail insurance program operations mitigates interest rate risk. This is accomplished by setting investing durations that match management's best estimate of when investments need to be liquidated to meet financial commitments.

LIQUIDITY RISK

Liquidity risk is the potential financial loss incurred if AFSC fails to meet its financial commitments for cash. In order to mitigate liquidity risks, the Corporation has in place sound cash management practices through cash flow statements, with the objective of maintaining sufficient funds to meet the business needs at all times. Liquidity risks are minimized through: retaining adequate bank balances in operating accounts which yield a reasonable rate of return through the Government of Alberta Consolidated Cash Investment Trust Fund, an investment portfolio which is structured in such a way that a portion of the portfolio is accessible at short notice, available access to advances from the Government of Alberta and borrowing through Alberta Finance with a revolving borrowing limit of \$1.2 billion.

INSURANCE RISK

AFSC's insurance operations mitigate insurance risk by setting premium rates that reflect actuarially sound business principles, by taking into consideration the results of the program and the amount of carried over surplus in the Insurance Fund.

To limit the exposure of the Provincial Treasury against losses significantly in excess of program premiums, management has secured government and private sector reinsurance arrangements for Production Insurance programs.

OPERATIONAL RISKS

Operational risk is inherent in all business activities of the Corporation and cannot be eliminated entirely. However, the risk is minimized through adequate internal process controls and in some cases insuring against operational risk.

An Enterprise Risk Management plan which includes identification and analysis of risks and measures, is in place to monitor and mitigate financial, market and operational risks and assists managers and staff in identifying and managing operational risk. In addition, Corporate policies and procedures are in place to ensure adequate internal controls exist to reduce the exposure to operational risk. Staff at all levels of the organization are responsible to comply with the policies and procedures and managers are responsible for managing operational risk in their respective work areas.

The Executive Management Team is responsible for managing Corporate wide enterprise risk, while the Board, through its Committees, oversees the management of risk.

Each core business is responsible for managing the operational risks by establishing appropriate internal process and system controls. Specialized Corporate functions such as finance, human resources, administration and information management are entrusted with management of operational risk specific to their areas. Finance manages risk related to interest rate, liquidity and financial controls. Human Resources helps other departments manage the risk related to employee recruitment, retention, succession planning and employee discipline. Administrative Services is responsible for managing risk associated with physical facilities & assets, employee safety and security, corporate liability and business continuity. Information Technology manages the risk related to computer information processing systems, electronic information, security, data integrity, disaster recovery and storage, retrieval, & destruction of electronic information.

As part of overall Corporate Enterprise Risk Management, the Internal Audit department plans and conducts operational and functional audits based on risk assessments. This group provides reports on adequacy

of internal process controls and compliance with policies and procedures. The external auditors review the effectiveness of internal controls in place to mitigate risk annually. Both external and internal audit report their findings to the Board Audit Committee.

INSURANCE

BUSINESS PROFILE

As one component of Alberta's business risk management strategy, AFSC's insurance programs continue to help producers meet the challenges of unpredictable weather and world commodity markets head on.

All AFSC insurance programs are voluntary and can be personalized to any farm business. Producers have a variety of programs to choose from to cover their production losses, including Production and area based Insurance (for annual crops), Hay Insurance (for perennial crops) or Hail Insurance. This year, AFSC reinstated enhanced Moisture Deficiency and Satellite Imagery programs for insuring native or improved perennial pastures.

2005-06 marked the third year that producers were able to cover market price risk through the Spring Price Endorsement (SPE) option of the Production Insurance program. This feature protects insured producers against significant drops in market prices between the time seeding decisions are made and when crops are harvested. Producers who purchase SPE coverage automatically receive Revenue Insurance Coverage (RIC) to help offset the effects of long-term low market prices.

To encourage participation in the 2005-06 crop year, the provincial share of premium contribution for SPE was increased from 50% to 70% and benefits under RIC for producers were increased from 50% to 70%.

PRODUCTION INSURANCE (PI)

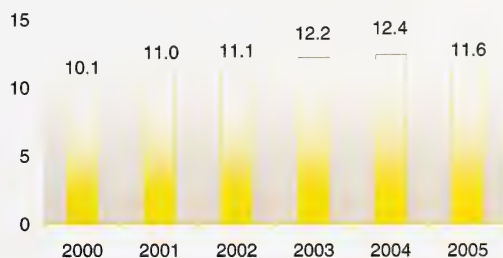
Producers who participate in AFSC's Production Insurance program have access to a variety of cost-effective strategies to manage their farming risks. Production Insurance provides a production guarantee on crop losses due to designated perils. Special features are available for producers who want increased income protection.

Production Insurance is available on grains and oilseeds, grain corn, sugar beets, vegetables, pulse crops, a number of specialty crops, and honey production. The Federal and Provincial governments support the Production Insurance program by paying all

administration expenses and sharing premium costs with producers. The producer's share of the premium varies according to the insurance coverage level they select (see funding information following).

Producers continue to view Production Insurance as an important risk management tool, with the number of contracts in 2005 dropping slightly to 14,575 for Production Insurance and 11,566 with the Hail Endorsement (HE). The number of acres insured through Production Insurance decreased marginally from 12.4 million in 2004 to 11.6 million in 2005. This decrease was as a result of areas of the province being too wet to seed, and as a result of producers' concerns over high premiums after the 2002 drought. 2005 insured acres are comparable to participation prior to the 2002 drought. Hail Endorsement uptake decreased similarly from 9.7 million acres insured in 2004 to 9.4 million acres in 2005.

**Production Insurance Acres Insured
2000 to 2005 (in millions)**



Premiums for Production Insurance (including HE and SPE) totaled \$292.6 million. With the continued concern for low market price outlooks and the increased SPE premium share contribution by the Provincial Government, SPE/RIC participation increased more than three times to 5,773 subscriptions. This is compared to 1,639 subscriptions in 2004.

However, producers faced the challenge of continued low commodity prices and delayed harvest from fall rains and early snows resulting in reduced yields and quality in the previous year. AFSC issued payments for SPE of \$22.6 million (2004-05 - \$6.4 million) and RIC of \$50.5 million (2004-05 - \$1.8 million) related to the 2005 crop as of March 31, 2006.

In many areas of the province, seeding was delayed by the need to harvest 2004 crop and spring rains. AFSC accepted 492 unseeded acreage claims and issued payments equal to \$2.0 million. Throughout the growing season, most areas experienced adequate to excessive rainfall. As a result of these conditions crop yields were above average.

In 2005-06, Production Insurance claims (including HE, SPE and RIC) totaled \$153.1 million, up from \$131.5 million the previous year.

Funding: Production Insurance is funded by premiums from producers, the Province of Alberta and the Government of Canada in accordance with the federal-provincial-territorial Agricultural Policy Framework Agreement. Premiums are funded 32% by producers, 45% by Alberta, and 33% by Canada. In addition, the Government of Canada funds 60% of the net administration and adjusting costs, with the Province of Alberta funding the remaining 40%.

A Crop Insurance Fund is established to account for all revenue and expenses related to the Production Insurance program, including claim payments. Over the last three years, the Province of Alberta has introduced a number of enhancements to Alberta's Production Insurance program. Some of these Alberta initiatives are not cost shared by the Federal Government, as they are considered inconsistent with the national program. The Production Insurance program results, in Schedule 1 of the Financial Statements, include both the national program and Alberta initiatives. The surplus balance of \$349.7 million in the Crop Insurance Fund is made up of a \$301.7 million surplus representing the national program, a \$33.6 million surplus representing Alberta initiatives and a surplus of \$14.4 million representing the Crop Reinsurance Fund of Alberta.

The Crop Reinsurance Fund of Alberta is the provincial counterpart to the Federal Crop Reinsurance Fund of Canada for Alberta. Surplus balances in these two funds and the Crop Insurance Fund determine the share of premiums to be transferred to the two reinsurance funds and how indemnities are funded from each fund. AFSC administers and accounts for the Provincial Reinsurance Fund, which is consolidated with the Crop Insurance Fund for financial statement purposes. The Government of Canada holds the Federal Reinsurance Fund. For the fiscal year ended March 31, 2006, \$11.6 million was contributed to the Crop Reinsurance Fund of Alberta and \$45.1 million was contributed to the Crop Reinsurance Fund of Canada for Alberta. A summary of transactions in the two reinsurance funds is under Note 17 to the Financial Statements.

HAY AND PASTURE INSURANCE

The Hay Insurance Program offers a specific production guarantee to producers. This insurance is available on an individual coverage basis and compensates for production losses on hay crops caused

by designated perils. To help stabilize coverage for producers who experienced multiple years of low yields compared to the risk area, AFSC introduced additional changes to individual coverage levels to reduce the impact of low yields ("enhanced cushioning").

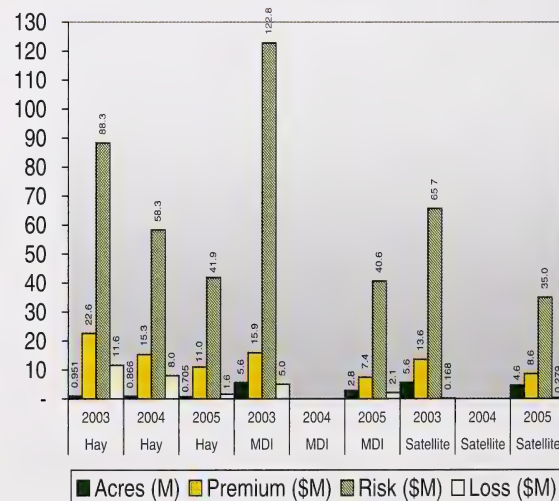
For 2005-06, Hay Insurance participation declined from the previous year, with 3,488 policies on 705,000 acres, compared to 4,164 policies and 866,000 acres in 2004-05. This was due to large carry over hay inventories and increased premium rates resulting from 2002 drought. Improved crop growth conditions resulted in \$1.6 million in losses compared to \$8.0 million in claims paid in 2004.

AFSC offered two distinct pasture programs for 2005-06. These programs provided considerably more options for producers to customize pasture coverage protection based on their needs. Satellite Imagery (SAT) Insurance Program, available only in selected areas in southern Alberta, is an area based (producers' township) insurance option that uses satellite imagery data to assess pasture conditions and determine payments.

SAT program enhancements included:

- 1) a long season option (added August); and
- 2) split season endorsement (to cover poor conditions in one part of the season).

HIGHLIGHTS OF HAY & PASTURE INSURANCE PROGRAM



The Moisture Deficiency Insurance (MDI) Program is a province wide, area based, insurance option that helps protect producers' pasture against a possible limited

accumulation of moisture at weather stations selected for insurance purposes. Producers can:

- 1) choose to include spring soil moisture;
- 2) select length and weights of coverage period; and
- 3) choose whether to purchase split season endorsement.

7.4 million acres were insured under both programs in 2005, compared to 11.2 million acres in 2003. No insurance programs were available for pasture in 2004.

Funding: Funding parameters are included with those provided for Production Insurance.

HAIL INSURANCE

Hail Insurance provides producers with affordable spot-loss protection for damage to crops due to hail or accidental fire. This coverage can be taken in addition to Production Insurance or on its own. Any individual with an interest in an insurable crop can participate, whether they are the producer, tenant or landlord with a crop share lease agreement. The combined dollar coverage of all insured parties cannot exceed the maximum dollar coverage per acre limit. Losses are paid based on the percentage of damage that occurs to the crop.

In the 2005 crop year, producers purchased 7,583 Hail Insurance policies which is a marginal increase from 2004. Insured acreage increased by 7.5% over 2004 to 5.6 million acres. Premiums increased by 18% with \$28 million premiums paid by producers. This increase was as a result of more producers purchasing Hail Insurance at elevated levels or dollar coverage, due to higher than expected average crop yields.

Losses were paid on 1,700 contracts for \$21.7 million with loss to premium ratio of 77.5%. This resulted in \$2.5 million of premiums being refunded to producers as the Hail Insurance fund was at the target level for actual soundness of the program.

WILDLIFE DAMAGE COMPENSATION

The Wildlife Damage Compensation program provides spot loss coverage for crop damage caused by waterfowl, big game animals, or upland game birds. Crops must be either standing or in swaths. Damage to stacked hay is covered in certain circumstances.

Wildlife damaged a significant number of the 2004 snowed under crops, resulting in an additional 1,115 claims and \$5.9 million being paid in the Spring of 2005.

Total losses for 2004 crop year were approximately \$12.2 million.

In most areas of the province, harvest in the fall of 2005 was delayed by rains and early snow resulting in 893 claims received on 2005 crop for losses of \$4.1 million.

Funding: Wildlife damage compensation is a grant program; consequently, no premiums are charged. However, a non-refundable appraisal fee of \$25 is charged for each section of land where damage has occurred. The Government of Alberta funds 52% of indemnities and the Government of Canada funds the remaining 48%. The Government of Canada funds 60% of the administration and adjusting costs and the Province of Alberta funds the remaining 40%.

AGRICULTURE INCOME STABILIZATION

BUSINESS PROFILE

The Canadian Agricultural Income Stabilization (CAIS) program is in its second year of delivery. The CAIS program is a federal-provincial-territorial initiative that provides both income stabilization and disaster assistance to producers of all types of agricultural commodities. CAIS provides coverage unique to every producer based on his or her industry, farming practices, and historical success. Designed to work with Production Insurance, the CAIS program is a key component of Alberta's business risk management strategy.

With benefits of over a half billion dollars paid out in Alberta to date to over 75% of Alberta's producers, the CAIS program is able to target payments to those producers who needed income support.

CANADIAN AGRICULTURAL INCOME STABILIZATION (CAIS) PROGRAM

The CAIS program requires producers to annually elect a level of protection. If a producer's claim year production margin (the difference between allowable income and allowable expenses) falls below their support level, they are eligible to receive government benefits. The support level is calculated using an Olympic average, by taking the production margins for the previous five years, dropping the highest and lowest, and averaging the remaining three margins.

Improvements made to the CAIS program nationally this year include extended deadlines and the removal of the producer deposit requirement. Based on input provided in stakeholder meetings conducted throughout the country, the deposit will be replaced by a fee that will commence for the 2006 program year. Any producer funds on deposit were returned, providing much needed operating funds during these difficult times in agriculture.

Alberta introduced the Reference Margin Pilot Project this year that will be applied to all 2003-2005 program year claims. The purpose of the pilot program was to determine whether reference margins could be stabilized in order to make the program respond better when disaster strikes. The pilot program will use the greater of the producer's average of the last three years of Production Margins or the Olympic average (national method of calculation of support levels).

Several improvements and innovations were made to the CAIS program this past year and these include: the automatic renewal of elected coverage levels, improved claim processing times, and innovative options developed for producers in an overpayment position. AFSC's customers will further benefit from improvements within the upcoming year with the launch of the new myAFSC website, as well as the implementation of the new CAIS program computer system.

Funding: The CAIS program is funded in accordance with the federal-provincial-territorial Agriculture Policy Framework (APF) Agreement. The Government of Canada funds 60% of claim payments and the costs of delivering the program, while the Alberta Government funds the remaining 40%. Any benefit payment to Alberta producers above the national program parameters, that is a result of an enhancement, is fully funded by the Alberta government. These enhancements include the Alberta 2003-2005 Reference Margin Pilot Project and the higher payment cap of \$5 million per diem (\$3 million nationally).



Rancher's Beef Ltd. – Balzac, AB

LENDING

BUSINESS PROFILE

Whether it's financing for a farm, or a commercial business, AFSC Lending is helping Albertans capitalize on solid business opportunities. With 51 offices across the province, AFSC's lenders are close to their customers and uniquely positioned to support economic growth in rural Alberta. Our lenders understand that accessing capital can be a challenge. By taking the time to understand customers' business needs, our lenders are able to customize a financing solution by providing a direct loan or helping source the necessary funds through other lenders. AFSC offers a wide variety of lending services, including Farm loans, Vendor Mortgage loans, Disaster Assistance loans, Guarantees, Commercial loans, Capital Sourcing and Export Financing.

In 2005 - 06 we reorganized and streamlined our resources but at the same time improved our customer service through our new hybrid lending model. Account Managers now can provide all lending programs (Farm and Commercial) to our customers.

The number of farm loans approved under the BFP and DFP increased by approximately 27% and our dollar volume by approximately 44% over the previous year, while maintaining our commercial business lending portfolio. Lending for all farm loan programs increased in excess of 18%.

BEGINNING FARMER PROGRAM (BFP)

The BFP provides stable, long-term funding to new entrants into farming or those bringing years of off-farm business experience to their farm venture. Producers who are expanding or diversifying their operations are also eligible for financing under this program, which continues to help rural Alberta develop new growth opportunities.

The BFP offers market-based interest rates and gives producers the option to fix the interest rate for the life of the loan or choose a 5-year renewable term.

The BFP provides an interest incentive of 1.5% for the first five years, with satisfactory compliance of program eligibility criteria.

The total amount advanced under the BFP in 2005-06 increased from the previous year, from \$80.1 million to \$116.3 million. The increased lending volume is due to economic conditions and uncertainty in the agriculture industry this past year. AFSC authorized a total of 794 BFP loans, an increase of approximately 29% from 2004-05, with an average loan amount of \$146,000.

DEVELOPING FARMER PROGRAM (DFP)

The DFP provides long-term loans with fixed interest rates to eligible primary producers whose farm operations are in a more advanced stage of development. The DFP offers borrowers market-based interest rates.

A total of \$4.1 million was authorized for 21 DFP loans, compared to 25 loans for \$3.6 million the previous year, with the average loan amount of \$195,000.

ALBERTA FARM LOAN PROGRAM (AFLP)

Effective April 1st, 2006, a new farm loan program was introduced replacing the Beginning Farmer and Developing Farmer programs. The new Alberta Farm Loan program will provide a consistent and reasonable source of loan capital to individuals and companies involved in primary agriculture in Alberta.

VENDOR MORTGAGE PROGRAM

Producers interested in exiting the agriculture industry can receive assistance through AFSC's Vendor Mortgage program. These loans can facilitate inter-generational transfer of farm operations by allowing the seller of a property/farm operation (usually, but not always, the buyer's parents) to finance a sale by holding the mortgage for the purchaser. AFSC acts as the vendor's agent and ensures repayment. Qualified buyers using the Vendor Mortgage program may be eligible for a maximum of 1.5% interest incentive under the BFP, for the first five years.

ALBERTA DISASTER ASSISTANCE LOAN PROGRAM (ADALP)

The Provincial Government makes ADALP loans available to help producers recover from severe losses during times of crisis. This program was designed as a standby emergency response program. It addresses a wide range of production and income-related losses and can be used to restore working capital and financial viability to an operation, through flexible terms and low interest rates. In 2005-06, AFSC authorized 84 ADALP loans totaling \$11.9 million, compared to 270 loans totaling \$29.9 million for the previous fiscal year. The reduction in loans under this program was due to fewer farm disasters and some recovery from the impact of the BSE crisis.

ALBERTA FARM DEVELOPMENT LOAN PROGRAM (AFDL)

The Alberta Farm Development Loan (AFDL) program services a wide range of producer needs for everything from capital to operating loans. It makes short, medium, and long-term financing available to producers at a reasonable cost for loans made through commercial lenders (chartered banks, ATB Financial and most credit unions) with repayment guaranteed by AFSC based on program terms and conditions. The AFDL is particularly beneficial where banks do not have specific programs available to service the producer's requirements.

COMMERCIAL LENDING

Following the lead of Alberta's entrepreneurs, AFSC continually looks for new and innovative ways to do business. AFSC's goal is to support and strengthen Alberta's rural and business communities. AFSC provides unique products not generally available through other financial institutions and we strive to be the lender of choice when Alberta entrepreneurs are looking for financing solutions. With our thorough understanding of business development and our innovative approach to financing that supports Alberta's business and agri-industry sectors, AFSC is helping build a strong, sustainable rural economy.

AFSC's expertise in the value-added agriculture and food processing sectors is well known. By enhancing existing programs or introducing new loan programs, we have been able to help the agri-industry develop additional slaughter capacity in Alberta. Two key initiatives in this regard were the Project Investor Financing Loan Program, which facilitates increased investment into beef slaughter projects and the Beef Product and Market Development Loan Program, which is intended to increase market opportunities for Alberta beef. Ten projects were approved through the year with a total value of \$12 million.

AFSC granted 179 loans to Alberta businesses in the last fiscal year totaling \$47.8 million. There were 93 agri-businesses assisted with a total investment value of \$97 million. Total rural businesses assisted were 207 with a total investment value of almost \$99 million. AFSC also supported 37 exporting businesses with a total investment value of \$65 million.

Funding: AFSC Lending programs are funded by short and long-term borrowing from the Province of Alberta. The province provides financing to AFSC on

terms similar to the provincial cost of borrowing. Operational costs for AFSC's lending operations are funded by interest and fees from customers and contributions from the province.

CORPORATE

AFSC is customer driven, committed to finding innovative ways to improve its delivery to more effectively meet the needs of our clients and staff. In 2005-2006 AFSC reviewed and enhanced service delivery in order to maintain an efficient and effective work force.

CUSTOMER SATISFACTION

Alberta's agriculture community is continuing to experience difficult times. High input costs associated with low commodity prices are continuously eroding margins. The Corporation managed to maintain a high level of corporate satisfaction at 67%, despite many challenges. Some of the challenges are attributed primarily to the lack of clarity and consistency in program parameters due to ongoing evolution of the CAIS program, which continued to change to meet the needs of producers. This led to continued delays in some program payments which, in turn, contributed to customer dissatisfaction with AFSC. Additionally, as a result of low commodity prices, crop insurance customers may have been less satisfied with the coverage they were able to purchase.

STAFF SATISFACTION

The past year has been challenging with AFSC embarking upon a corporate wide business transformation and successfully completing process reviews for most divisions of the Corporation. An initial period of uncertainty and change caused anxiety and apprehension in some employees. However, the ensuing results have been positive and are expected to continue.

The Corporation is pleased that 87% of staff are satisfied with AFSC as an employer, despite the fact that this survey was done in the midst of restructuring of major divisions in the Corporation.

We continue to focus on the results of our annual staff satisfaction survey, ensuring that staff concerns are addressed wherever possible. A staff conference in Red Deer in early February 2006 was well received. This was an excellent opportunity to bring all AFSC staff together to plan for the future – a future focused on excellence, as we strive to become a provider of choice, an employer of choice and a partner of choice. Feedback received from staff at the conference and from a staff satisfaction survey provided at the conference, will be used to ensure that AFSC continues to be a great place to work and to conduct business.

Our "hiring for the future" strategy continues to be of paramount importance. In addition to external recruitment campaigns, AFSC has once again offered several in-house training sessions to develop staff skills in supervision, leadership and management. The Corporation will continue to focus on retention and succession planning in the coming year. Maintaining a positive work environment will ensure that AFSC continues to be a great place to work.



GOALS AND PERFORMANCE

AFSC takes an active approach to business planning by setting out goals, strategies and targets in three-year cycles and reviewing the plans annually. Business operation goals in Insurance, CAIS, and Lending are also linked to the overall AAFRD Business Plan goals. As part of this Management Discussion and Analysis, goals and their performance measures are presented, based on the three goals outlined in AFSC's 2005-2008 Business Plan.

Goal 1: Growth

AFSC will encourage the growth and development of Alberta's small businesses, farms and value-added agriculture businesses by providing unique financial services.

Key Results	Measure	Performance	Target
Commercial: Investment in Alberta businesses including agri-business, rural business and Alberta-based exporters*	Total dollars invested in Alberta businesses	\$173 million	\$120 million
	Investment in agri-business	\$97 million	\$30 million
	Investment in rural business	\$99 million	\$80 million
	Investment in business exporting.	\$65 million	\$22 million
	Total number of businesses assisted	271	395
	Number of agri-businesses assisted	93	90
	Number of rural businesses assisted	207	320
	Number of businesses assisted that export	37	48
Farm Lending: Growth and development of farms	Number of loans	914	900
	Total loan amount	\$134 million	\$133 million
	Number of financial consultations	561	1,600

The number of financial consultations was lower than targeted because the responsibility for this service was transferred to AAFRD Commercialization Branch.

The Corporation met or exceeded the targeted performance measures, except for the number of businesses assisted under Commercial Lending. This was due to a higher than expected increase in the average capital investment by applicants.

Goal 2: Sustainability

AFSC will contribute to the sustainability of the agriculture economy by developing and providing unique risk management services.

Key Results	Measure	Performance	Target
Increased participation by farmers using risk management products.	Percentage of farmers that participate in either Production Insurance, CAIS or both.	Production Insurance - 50% CAIS - 66%	2005-06 will represent the Benchmark year.
Farmers continuously participate in risk management products.	Percentage of farmers that continue participation in risk management products.	Production Insurance - 96% CAIS 97%	90%
Risk management products are targeted to cover important risks identified by farmers.	Percentage of producers surveyed agree that they have business management products available to address risks.	66%* of insurance customers agreed that AFSC provides products that cover important risks.	78%
	Percentage of seeded acres for which Production Insurance products are available to total seeded acres.	There are insurance products available for 99.8%	95%

*The target in respect of products availability to cover important risks of producers was not met, which may have been due to producers immediate concerns about higher input costs and lower commodity prices, particularly in the grains and oilseeds sectors.

Goal 3: Efficiency

AFSC will be efficient and innovative in its operations while maintaining a high level of customer service.

Key Results	Measure	Performance	Target
AFSC programs are delivered effectively	Overall customer satisfaction with delivery of programs based on customer satisfaction survey results	67%*	80%
AFSC programs are delivered efficiently	Production Insurance work units per full-time equivalent employee (FTE)	802 work units per FTE. (774 work units per FTE in 2004 - 05)	Same or higher than the previous year
	Farm lending work units per full-time equivalent employee (FTE)	782 work units per FTE. (727 work units per FTE in 2004 - 2005)	Same or higher than the previous year
	CAISP work units per full-time equivalent employee (FTE)	14,108 work units per FTE. (9,951 work units per FTE in 2004-05)	Same or higher than the previous year
	Commercial lending work units per full-time equivalent employee (FTE)	194 work units per FTE. (233 work units per FTE in 2004 2005) The merger of farm and commercial lending during the year resulted in many joint activities that made it difficult to track lending work units completely accurately	Same or higher than the previous year
AFSC employees have a high degree of overall job satisfaction	Satisfaction rate of AFSC employees as measured by staff survey	87%	84%
Reduced administration costs	Total administration costs	In 2005-06 total administration expenses were \$58,101 (Previous Year \$60,019)	Not to exceed the amount in the previous business plan

*Some of the challenges are attributed primarily to the lack of clarity and consistency in program parameters due to ongoing evolution of the CAIS program, which continued to change over the course of the year to meet the needs of producers.

SUMMARY OF INSURANCE

AS AT MARCH 31, 2006

PRODUCTION INSURANCE FOR ANNUAL CROPS⁽¹⁾

CROP INSURANCE

Crop Year	Number of Contracts	Acres ,000	Risk \$,000	Premium \$,000	Contracts with Losses	Loss \$,000	Loss/ Premium Percent
2001	15,208	10,998	1,252,115	133,619	7,796	204,513	153.1
2002	15,082	11,100	1,489,980	155,968	12,198	667,882	428.2
2003	16,826	12,229	1,677,528	207,040	6,518	93,352	45.1
2004	16,443	12,387	1,458,942	215,760	4,753	52,654	24.4
2005	14,575	11,589	1,223,844	186,013	3,519	35,608	19.1

⁽¹⁾ Totals are for Production Insurance, Processing Vegetables, Honey, Corn Heat Units, Second Year Fescue (2001) and Silage/Greenfeed(2002-2004)

HAIL ENDORSEMENT⁽²⁾

Crop Year	Number of Contracts	Acres ,000	Risk ,000	Premium \$,000	Contracts with Losses	Loss \$,000	Loss/ Premium Percent
2001	12,688	9,278	1,096,037	46,067	2,485	39,079	84.8
2002	12,065	8,860	1,256,050	51,482	1,474	33,663	65.4
2003	12,824	9,343	1,356,025	65,996	2,742	52,255	79.2
2004	12,736	9,717	1,207,471	60,243	3,641	70,709	117.4
2005	11,566	9,353	1,042,368	53,441	2,783	44,361	83.0

⁽²⁾ Totals are for Production Insurance, Processing Vegetables, Honey, Corn Heat Units, Second Year Fescue (2001) and Silage/Greenfeed(2002-2004)

SPRING PRICE ENDORSEMENT⁽³⁾ (SPE)

Crop Year	Number of Contracts	Acres ,000	Risk \$,000	Premium \$,000	Contracts with Losses	Loss \$,000	Loss/ Premium Percent
2003	5,582	4,094	582,581	40,048	4,997	80,152	200.1
2004	1,639	756	81,994	5,605	1,356	6,383	113.9
2005	5,773	4,432	451,014	53,189	3,143	22,606	42.5

⁽³⁾ Includes Production Insurance and Silage/Greenfeed

REVENUE INSURANCE COVERAGE⁽⁴⁾ (RIC)

Crop Year	Number of Contracts	Acres ,000	Risk \$,000	Premium \$,000	Contracts with Losses	Loss \$,000	Loss/ Premium Percent
2003	5,582	4,094	582,581	N/A	0	0	N/A
2004	1,639	756	81,994	N/A	1,126	1,793	N/A
2005	5,773	4,432	451,014	N/A	5,615	50,537	N/A

⁽⁴⁾ Includes Production Insurance and Silage/Greenfeed

PRODUCTION INSURANCE FOR PERENNIAL CROPS

HAY INSURANCE

<i>Crop Year</i>	<i>Number of Contracts</i>	<i>Acres ,000</i>	<i>Risk \$,000</i>	<i>Premium \$,000</i>	<i>Number of Losses</i>	<i>Loss \$,000</i>	<i>Loss/ Premium Percent</i>
2001	1,949	453	30,444	6,769	1,575	14,413	212.9
2002	2,977	658	54,126	11,522	2,460	35,786	310.6
2003	4,618	951	88,285	22,645	1,523	11,588	51.2
2004	4,164	866	58,330	15,286	1,575	8,040	52.6
2005	3,488	705	41,874	10,918	480	1,612	14.8

SATELLITE IMAGERY INSURANCE (PASTURE)⁽⁵⁾ (SAT)

<i>Crop Year</i>	<i>Number of Contracts</i>	<i>Acres ,000</i>	<i>Risk \$,000</i>	<i>Premium \$,000</i>	<i>Number of Losses</i>	<i>Loss \$,000</i>	<i>Loss/ Premium Percent</i>
2001	677	2,056	18,687	3,446	677	16,097	467.1
2002	1,989	5,591	59,016	11,220	1,700	29,775	265.4
2003	1,980	5,634	65,737	13,626	67	168	1.2
2005	1,375	4,574	35,018	8,570	133	279	3.3

⁽⁵⁾ Pilot project for 2001 - not offered in 2004

MOISTURE DEFICIENCY INSURANCE (PASTURE)⁽⁶⁾ (MDI)

<i>Crop Year</i>	<i>Number of Contracts</i>	<i>Acres ,000</i>	<i>Risk \$,000</i>	<i>Premium \$,000</i>	<i>Number of Losses</i>	<i>Loss \$,000</i>	<i>Loss/ Premium Percent</i>
2002	3,882	3,464	44,695	5,581	2,891	23,733	425.2
2003	7,044	5,613	122,771	15,920	2,032	5,024	31.6
2005	3,121	2,791	40,578	7,406	1,021	2,061	27.8

⁽⁶⁾ Not offered in 2004

HAIL INSURANCE

<i>Crop Year</i>	<i>Number of Contracts</i>	<i>Acres ,000</i>	<i>Risk \$,000</i>	<i>Premium⁽⁷⁾ \$,000</i>	<i>Number of Losses</i>	<i>Loss \$,000</i>	<i>Loss/ Premium Percent</i>
2001	6,243	3,406	332,664	15,400	1,002	11,182	72.6
2002	5,105	3,051	295,411	13,434	797	10,219	76.1
2003	6,109	3,808	375,134	17,138	1,063	12,319	71.9
2004	7,489	5,225	498,753	23,737	2,117	32,293	136.0
2005	7,583	5,616	562,914	28,047	1,700	21,697	77.4

⁽⁷⁾ Before Premium refunds due to the favorable loan/premium ratio.

WILDLIFE DAMAGE COMPENSATION AND EXCRETA PROGRAMS

<i>Crop Year</i>	<i>Number of Wildlife Losses</i>	<i>Wildlife Loss \$,000</i>	<i>Number of Waterfowl Losses</i>	<i>Waterfowl Loss \$,000</i>	<i>Total Number of Losses</i>	<i>Total Loss \$,000</i>
2001	420	1,564	167	1,035	587	2,599
2002	749	3,984	335	1,996	1,084	5,980
2003	605	2,520	129	552	734	3,072
2004	1,524	7,792	684	4,356	2,208	12,148
2005	438	2,383	455	1,718	893	4,101

SUMMARY OF CANADIAN AGRICULTURAL INCOME STABILIZATION PROGRAM (CAISP)

AS AT MARCH 31, 2006

<i>Claim Year</i>	<i>Number of Claims Elected</i>	<i>Support Level \$,000,000</i>	<i>Number of Claims Processed</i>	<i>Number of Claims with Payment</i>	<i>Total Payment \$ 000,000</i>	<i>Average Payment \$</i>
2003	34,809	2,761	30,220	18,975	466	24,576
2004	35,433	2,738	15,788	8,454	152	18,018
2005	7,051	224	447	180	8	45,445

The above information reflects actual transactions up to March 31, 2006, while information in the Financial Statements includes adjustments, such as accruals.

SUMMARY OF LENDING

AS AT MARCH 31, 2006

	Authorizations 2005 – 2006		Authorizations 2004 – 2005		Accumulated Authorizations Jun '72 – Mar 2006		Active and Outstanding Mar 31, 2006	
	No.	\$M.	No.	\$M.	No.	\$M.	No.	\$M.
FARM DIRECT LOANS								
Beginning Farmer	794	116.3	616	80.1	22,632	2,503.6	7,852	663.0
Developing Farmer	21	4.1	25	3.6	634	69.2	149	22.7
Disaster Assistance	84	11.9	270	29.9	3,277	249.4	1,466	115.5
Other	15	1.9	0	0.0	5,304	280.8	107	5.6
SUBTOTAL	914	134.2	911	113.6	31,847	3,103.0	9,574	806.8
FARM GUARANTEES								
Alberta Farm Development Loans	180	11.5	299	16.2	169,304	2,294.8	2,186	56.2
Other Guaranteed Loans	1	0.6	1	0.2	2,491	116.7	13	1.1
Subtotal	181	12.1	300	16.4	171,795	2,411.5	2,199	57.3
TOTAL FARM	1,095	146.3	1,211	130.0	203,642	5,514.5	11,773	864.1
COMMERCIAL LOANS								
Direct Loans	179	47.7	253	63.6	10,824	1,395.5	1,026	172.8
Specific Guaranteed Loans	5	2.4	11	3.1	544	214.7	20	0.1
Alliance Lending	71	123.2	43	171.9	464	834.1	0	0.0
TOTAL COMMERCIAL	255	173.3	307	238.6	11,832	2,444.3	1,046	172.9
Corporate Grand Total	1,350	319.6	1,518	368.6	215,474	7,958.8	12,819	1,037.0

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying financial statements of Agriculture Financial Services Corporation and all other information relating to the Corporation contained in this annual report are the responsibility of management. The financial statements have been prepared in conformity with Canadian generally accepted accounting principles, using methods appropriate for the industry in which the Corporation operates and necessarily include some amounts that are based on informed judgments and best estimates of management. The financial information contained elsewhere in this annual report is consistent with that in the financial statements.

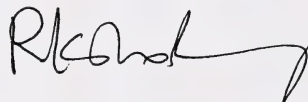
Management is responsible for maintaining a system of internal controls designed to provide reasonable assurance as to the reliability of financial information and to ensure corporate assets are safeguarded and liabilities are recognized. The internal control systems are augmented by periodic reviews by the Corporation's internal auditors.

The Alberta Auditor General is responsible to express a professional opinion on these financial statements.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Board of Directors exercises this responsibility through the Audit Committee, composed of directors who are not employees of the Corporation. The Audit Committee meets regularly with management, the internal auditors and the external auditors to discuss auditing and financial matters, to gain assurance that management is carrying out its responsibilities and to review and approve the financial statements. The internal and external auditors have full and free access to the Audit Committee.



Brad Klak
President and Managing Director



R. (Krish) Krishnaswamy, C.M.A.
Vice-President, Finance



Photo Courtesy of Lacombe Globe

Agriculture Financial Services Corporation

AUDITOR'S REPORT



To the Board of Directors of the Agriculture Financial Services Corporation

I have audited the balance sheet of the Agriculture Financial Services Corporation as at March 31, 2006 and the statements of revenue, expense and surplus, and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at March 31, 2006 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

A handwritten signature in black ink, appearing to read "Fred J. Deum".

FCA
Auditor General

Edmonton, Alberta
May 12, 2006

Agriculture Financial Services Corporation

BALANCE SHEET

AS AT MARCH 31, 2006

(IN THOUSANDS)

	2006	2005
ASSETS		
Cash	\$ 163,415	\$ 75,456
Accounts receivable (Note 4)	137,103	120,904
Due from Province of Alberta	8,028	50,669
Due from Government of Canada	330,914	293,189
Loans receivable (Note 5)	973,084	977,460
Investments (Note 6)	238,459	171,229
Property and equipment (Note 7)	32,012	26,747
	<u>\$ 1,883,015</u>	<u>\$ 1,715,654</u>

LIABILITIES AND SURPLUS

Accounts payable and accrued liabilities	\$ 25,371	\$ 31,481
Estimated indemnities payable (Note 8)	456,883	449,849
Due to Crop Reinsurance Fund of Canada for Alberta	16,630	13,737
Allowance for losses on loan guarantees (Note 14)	824	1,186
Notes payable (Note 9)	897,059	910,653
Deferred revenue (Note 10)	23,867	21,935
	<u>1,420,634</u>	<u>1,428,841</u>
Surplus	<u>462,381</u>	<u>286,813</u>
	<u>\$ 1,883,015</u>	<u>\$ 1,715,654</u>

Contingencies and commitments (Note 14)

The accompanying notes and schedules are part of these financial statements.

Approved by the Board:



Barry Holmes, Chair of Audit Committee



Bob Splane, Chair of the Board

Agriculture Financial Services Corporation

STATEMENT OF REVENUE, EXPENSE AND SURPLUS

FOR THE YEAR ENDED MARCH 31, 2006

(IN THOUSANDS)

	2006		2005
	<u>Budget</u>	<u>Actual</u>	<u>Actual</u>
	(Note 3(a))	(Schedule 1)	
Revenue:			
Premiums from insured persons	\$ 157,121	\$ 141,524	\$ 135,941
Interest	79,185	68,636	71,242
Contribution from Province of Alberta	276,950	468,033	319,922
Contribution from Government of Canada	308,653	290,918	431,378
Investment income	6,809	14,228	10,022
Fees and other income	4,778	4,775	5,374
Reinsurance recoveries	-	10	2,163
	<u>833,496</u>	<u>988,124</u>	<u>976,042</u>
Expense:			
Indemnities	657,803	638,984	720,436
Reinsurance	43,518	58,559	44,889
Administration, Schedule 2	61,551	58,101	60,019
Interest	53,279	45,027	45,647
Adjusting	7,484	7,646	8,072
Farm loan incentives	5,791	4,883	5,077
(Recovery) provision for doubtful accounts and for losses (Note 13)	2,426	(2,877)	1,595
Selling commissions	<u>2,470</u>	<u>2,233</u>	<u>2,027</u>
	<u>834,322</u>	<u>812,556</u>	<u>887,762</u>
Surplus (deficit) for the year	<u>\$ (826)</u>	175,568	88,280
Surplus at beginning of year		<u>286,813</u>	<u>198,533</u>
Surplus at end of year		<u>\$ 462,381</u>	<u>\$ 286,813</u>

The accompanying notes and schedules are part of these financial statements.

Agriculture Financial Services Corporation

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED MARCH 31, 2006

(IN THOUSANDS)

	<u>2006</u>	<u>2005</u>
Operating activities:		
Surplus for the year	\$ 175,568	\$ 88,280
Changes not affecting cash	(1,755)	1,700
Changes in assets and liabilities relating to operations	<u>(8,427)</u>	<u>3,208</u>
Net cash provided by operating activities ⁽¹⁾	<u>165,386</u>	<u>93,188</u>
Investing activities:		
Proceeds from repayments of loans receivable and sale of properties	190,132	181,109
Loan disbursements	(184,190)	(171,973)
Purchase of investments	(680,013)	(523,780)
Proceeds on disposal of investments	614,452	454,501
Purchase of property and equipment	(11,171)	(9,494)
Proceeds on disposal of property and equipment	<u>517</u>	<u>381</u>
Net cash utilized by investing activities	<u>(70,273)</u>	<u>(69,256)</u>
Financing activities:		
Borrowing from the Province of Alberta	568,581	1,828,362
Repayment of borrowing from the Province of Alberta	(584,385)	(1,840,186)
Government of Canada funding for property and equipment	3,432	619
Province of Alberta funding for property and equipment	<u>5,218</u>	<u>954</u>
Net cash utilized by financing activities	<u>(7,154)</u>	<u>(10,251)</u>
Net increase in cash from operating, investing and financing activities	87,959	13,681
Cash at beginning of year	<u>75,456</u>	<u>61,775</u>
Cash at end of year	<u><u>\$ 163,415</u></u>	<u><u>\$ 75,456</u></u>

⁽¹⁾ Net cash provided by operating activities includes \$43,184 (2005 \$47,533) of interest paid.

The accompanying notes and schedules are part of these financial statements.

Agriculture Financial Services Corporation

NOTES TO THE FINANCIAL STATEMENTS

MARCH 31, 2006
(IN THOUSANDS)

NOTE 1

AUTHORITY AND PURPOSE

The Agriculture Financial Services Corporation (the "Corporation") operates under the authority of the Agriculture Financial Services Act, Chapter A-12 RSA 2000.

The Corporation provides lending and insurance services and compensation programs. Its core programs and services include loans to beginning farmers, commercial lending, crop insurance, hail insurance and agricultural income stabilization payments. It also delivers other programs and services including loans to developing farmers, disaster loans, loan guarantees, and business counseling.

NOTE 2

SIGNIFICANT ACCOUNTING POLICIES AND REPORTING PRACTICES

These financial statements are prepared in accordance with Canadian generally accepted accounting principles.

(a) Cash

Cash consists of a deposit in the Consolidated Cash Investment Trust Fund which is managed by the Province of Alberta to provide competitive interest income while maintaining maximum security and liquidity of depositors' capital.

(b) Investments

Investments are carried at cost or amortized cost unless there is an other than temporary decline in the value of the investments, then the investments are written down to recognize the loss. Premiums and discounts on investments are amortized to investment income using the straight-line method over the period to maturity of the related investment. Gains and losses realized on disposal of investments are included in investment income.

(c) Property and Equipment

Property and equipment are carried at cost less accumulated amortization. Amortization is recorded on a straight-line basis over the estimated useful lives of the assets as follows:

Building	25 - 40 years
Land improvements	25 years
Software development costs	2 - 10 years
Equipment and furniture	10 years
Vehicles	5 years
Computer equipment	5 years

(d) Notes Payable

Notes payable are carried at amortized cost. Premiums and discounts on notes payable are amortized to interest expense using the effective yield method over the period to maturity.

Agriculture Financial Services Corporation

NOTE 2

SIGNIFICANT ACCOUNTING POLICIES AND REPORTING PRACTICES (CONTINUED)

(e) Fair Value of Financial Instruments

Because of the relatively short period to maturity, short-term financial instruments are valued at cost and adjusted for any applicable allowance for doubtful accounts. This is considered to be equivalent to fair value and applies to Cash, Accounts receivable, Due from Province of Alberta, Due from Government of Canada, Accounts payable and accrued liabilities, Estimated indemnities payable and Due to Crop Reinsurance Fund of Canada for Alberta. Fair values of Loans receivable, Investments and Notes payable are disclosed in their respective notes.

(f) Reinsurance

In accordance with the Federal/Provincial Agricultural Policy Framework Implementation Agreement, two crop reinsurance funds were established. On behalf of the Province, the Corporation administers the provincial fund called the Crop Reinsurance Fund of Alberta. Canada holds the federal fund called the Crop Reinsurance Fund of Canada for Alberta. The Crop Reinsurance Fund of Alberta is included as part of the crop insurance surplus of the Corporation. Contributions to and withdrawals from the Funds are made in accordance with terms and conditions of the agreement (see Note 17).

Estimates of amounts recoverable from non-government reinsurers on premiums, indemnities and adjusting expenses are recorded in Accounts receivable. Reinsurance recoveries are not netted against indemnities, they are separately disclosed under revenue. Reinsurance expenses are not netted against premiums from insured persons or contributions from the Province and Government of Canada; they are separately disclosed under expenses.

(g) Loan Discounting

Loans made under the Alberta Disaster Assistance Loan Program, Alberta Farm Income Disaster Program, and amounts previously deferred under the Indexed Deferral Plan are discounted when they involve significant concessionary elements. The amounts discounted are being amortized to revenue over the lives of the concessionary terms.

(h) Revenue Recognition

Interest revenue on loans receivable is recognized on an accrual basis unless the ultimate collectability of the loan is in doubt. When a loan is classified as impaired, interest revenue is no longer recognized. An impaired loan is a loan in which there is risk of loss to the Corporation for full and timely collection of the debt. Impairment may be due to a security deficiency, inadequate cash flow, economic factors in a specific segment of the industry or a catastrophic event.

Premiums from insured persons, including federal and provincial government contributions, are recognized as income when invoiced to producers.

Agriculture Financial Services Corporation

NOTE 2

SIGNIFICANT ACCOUNTING POLICIES AND REPORTING PRACTICES (CONTINUED)

(h) Revenue Recognition (continued)

Federal and provincial contributions for property and equipment acquisitions are recorded as deferred revenue until that revenue is recognized on the same basis as those property and equipment costs are amortized.

Loan fees are recognized when received or at the time of loan disbursement. Other fees are recorded when the Corporation completes the applicable service.

(i) Pensions

The Corporation participates in multi-employer pension plans with related government entities. Pension costs included in these statements comprise the cost of employer contributions for current service of employees during the year.

(j) Provision for Losses on Loans and Guarantees

Provisions are established for specifically identified potential losses on loans and guarantees as well as for anticipated but not specifically identified losses. When a loan is identified as impaired, a specific provision is established. Specific provisions are established by reducing the recorded investment in the loan by the discounted fair value of the security and the estimated costs to collect. Specific provisions are determined in this manner because the amounts and timing of future cash flows cannot be estimated with reasonable reliability. The provision for doubtful accounts is adjusted for the change in the present value of the security held.

The majority of the Corporation's loan portfolio is with beginning and developing business operations and hence, is subject to high risk. The Corporation recognizes this by providing significant general allowances for doubtful accounts. In establishing the general component of the allowance, management estimates loss percentages based on risks and applies them to loans receivable balances. Risk is based on land value trends, the impact of federal and provincial government programs, international trade criteria, future commodity price trends, climatic conditions and the financial stability of the borrower.

(k) Transactions with Related Parties

The Province and the Government of Canada significantly influence the programs delivered by the Corporation and are major contributors to the funding of the programs. Therefore, both governments are considered related parties. All related party transactions with the Province and the Government of Canada have been recorded at the amount of consideration paid or received as agreed to by the related party (see Note 16).

Agriculture Financial Services Corporation

NOTE 3

FINANCIAL STRUCTURE

(a) Budget

The Board of Directors approved the Corporation's budget in August 2004. Contribution from the Province of Alberta of \$276,950 was authorized by the Legislative Assembly and is reflected in the Corporation's budget approved by the Board. The budgeted contribution from the Province of Alberta was adjusted by \$44 for deferred revenue.

(b) Crop Fund Balance Restriction

In accordance with the Federal/Provincial Agricultural Policy Framework Implementation Agreement, the crop insurance fund is restricted to being used for crop insurance purposes.

(c) Other Revenue and Expenses

The Other column in the Schedule of Revenue, Expense and Surplus includes the wildlife program, the Farm Income Disaster Program and consulting fees and expenses that are not attributable to any of the programs disclosed in the Schedule.

NOTE 4

ACCOUNTS RECEIVABLE

	<u>2006</u>	<u>2005</u>
Canadian Agricultural Income		
Stabilization program:		
Overpayments and advances	\$ 123,076	\$ 105,640
Administration fees	2,439	2,612
Premiums from insured persons:		
Crop insurance program	9,917	12,432
Hail insurance program	351	265
Prepaid expenses	617	692
Other	<u>2,085</u>	<u>392</u>
	138,485	122,033
Less allowances for doubtful accounts		
(Note 13)	<u>(1,382)</u>	<u>(1,129)</u>
	<u>\$ 137,103</u>	<u>\$ 120,904</u>

Included in Canadian Agricultural Income Stabilization (CAIS) program overpayments and advances of \$123,076 are \$88,502 in estimated overpayments that are subject to measurement uncertainty. The amount could change substantially in the future if factors considered by management in establishing the estimate for

Agriculture Financial Services Corporation

NOTE 4

ACCOUNTS RECEIVABLE (CONTINUED)

the CAIS program overpayments were to change significantly. The estimate of \$88,502 is for CAIS participants who received advance payments but who have not yet had their final claim processed by the Corporation. The estimate is based on historical experience.

CAIS overpayments are non-interest bearing until December 31, 2006. Participants will receive a rebate if they repay the CAIS overpayment within 90 days of the overpayment notification or they can convert the overpayment to an interest bearing loan up until December 31, 2006. If the overpayment is not repaid or converted to a loan, the Corporation will pursue collection. Collection will include the recovery of the overpayment from future payments under the programs delivered by the Corporation as well as programs administered by the Province of Alberta and Government of Canada.

NOTE 5

LOANS RECEIVABLE

Loans receivable are comprised of the following:

	2006			2005	
	Recorded Investment	Specific Allowance	General Allowance	Net Carrying Value	Net Carrying Value
Farm lending	\$ 815,661	\$ (846)	\$ (25,419)	\$ 789,396	\$ 790,743
Commercial lending	173,742	(8,358)	(2,805)	162,579	165,556
	<u>\$ 989,403</u>	<u>\$ (9,204)</u>	<u>\$ (28,224)</u>	951,975	956,299
Accrued interest				24,946	25,701
Accrued incentives				(2,279)	(2,451)
Loan discounts				(1,558)	(2,089)
				<u>\$ 973,084</u>	<u>\$ 977,460</u>

Impaired loans included in the preceding schedule:

	2006			2005	
	Recorded Investment	Specific Allowance	Net Carrying Value	Net Carrying Value	
Commercial lending	\$ 19,852	\$ (8,358)	\$ 11,494	\$ 7,795	
Farm lending	6,268	(846)	5,422	3,999	
	<u>\$ 26,120</u>	<u>\$ (9,204)</u>	<u>\$ 16,916</u>	<u>\$ 11,794</u>	

Agriculture Financial Services Corporation

NOTE 5

LOANS RECEIVABLE (CONTINUED)

The impaired loans balance includes property held for sale which has been acquired as a result of foreclosures, quit claims and other actions. There is a specific allowance of \$2,688 (2005 \$2,518) on property balances outstanding of \$3,941 (2005 \$3,691).

Loans receivable does not include prepaid balances \$12,609 (2005 \$12,668) which are included in Accounts payable and accrued liabilities.

Included in the above loans receivable balance are loans with concessionary terms which, before discounting, have principal amounts outstanding of:

	2006	2005
		(Restated)
Alberta Disaster Assistance Loan Program	\$ 40,239	\$ 45,048
Alberta Farm Income Disaster loans	21,939	27,628
Indexed Deferral Plan	668	809
	<u>\$ 62,846</u>	<u>\$ 73,485</u>

The prior year concessionary loans were restated because the amounts previously included an amount that did not have concessionary terms.

Loans receivable of \$973,084 is subject to measurement uncertainty. The amount established for specific and general allowances of \$37,428 to cover estimated losses on loans (see Note 2(j)) could change substantially in the future, if factors considered by management in establishing these estimates were to change significantly.

The approximate fair value of loans receivable at March 31, 2006 is \$981,203 (2005 \$967,192). Fair value is based on future cash flows discounted by rates equivalent to the market rates on loans with similar terms and credit risk.

NOTE 6

INVESTMENTS

Bonds and debentures:

	2006	2005
Government of Canada, direct and guaranteed	\$ 141,546	\$ 124,308
Other provincial direct and guaranteed	15,742	14,293
	<u>157,288</u>	<u>138,601</u>
Corporate securities	78,520	31,075
	<u>235,808</u>	<u>169,676</u>
Accrued interest	2,651	1,553
	<u>\$ 238,459</u>	<u>\$ 171,229</u>

Agriculture Financial Services Corporation

NOTE 6

INVESTMENTS (CONTINUED)

The fair value of investments at March 31, 2006 is \$238,183 (2005 \$173,697). Fair value is based on quoted market prices including accrued interest.

NOTE 7

PROPERTY AND EQUIPMENT

	2006		2005	
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
Software development costs	\$ 34,448	\$ 14,980	\$ 19,468	\$ 13,459
Building	9,341	1,873	7,468	7,577
Computer equipment	7,958	6,207	1,751	2,064
Equipment and furniture	4,325	2,242	2,083	2,483
Vehicles	1,401	940	461	494
Land and land improvements	799	18	781	670
	<u>\$ 58,272</u>	<u>\$ 26,260</u>	<u>\$ 32,012</u>	<u>\$ 26,747</u>

Software development costs include \$7,126 (2005 \$3,983) of costs incurred that are not amortized because they are still in the developmental or construction stage.

NOTE 8

ESTIMATED INDEMNITIES PAYABLE

	2006	2005
Canadian Agricultural Income Stabilization program	\$ 449,222	\$ 408,064
Crop insurance	6,654	28,761
Wildlife compensation	826	12,573
Hail insurance	181	451
	<u>\$ 456,883</u>	<u>\$ 449,849</u>

Agriculture Financial Services Corporation

NOTE 8

ESTIMATED INDEMNITIES PAYABLE (CONTINUED)

Estimated indemnities payable of \$449,222 and corresponding contributions and receivables from the Province of Alberta and Government of Canada for the Canadian Agricultural Income Stabilization (CAIS) program are subject to measurement uncertainty because they could change significantly in the future, if factors considered by management in establishing the estimates were to change significantly.

CAIS indemnities payable includes estimated payments for the 2005 claim years of \$318,310 for the vast majority of claims that have not been received yet because the deadline for submission of complete information is after the end of the fiscal year. CAIS program payments are triggered when the participants claim year program margin falls below their support level.

The two factors impacting estimated indemnities payable for the 2005 claim year are the number of participants and estimated program margins. The estimated number of participants for the 2005 claim year is based on the number of farm operations participating in the program during the 2004 claim year. The estimated program margins are based on forecasted changes in eligible income and expenses and inventories between 2004 and 2005. If the 2005 estimated program margins were to increase by 5%, the estimated indemnities payable for the 2005 claim year would decrease by \$12,000. If the 2005 program margins were to decrease by 5% the estimated indemnities payable for the 2005 claim year would increase by \$14,000.

CAIS indemnities payable includes estimated payments of \$46,010 for claims received but not processed for the 2003 and 2004 claim years. The estimates for the 2003 and 2004 claim years are based on the number of claims received but not yet processed and the estimated average payment per claim.

CAIS indemnities payable for the 2003, 2004 and 2005 claim years also includes estimated payments of \$84,902. The estimate is for claims not yet processed that may receive an increased payment as a result of a change in the method used to determine support levels. The estimate is based on the historical payment ratio for claims processed.

NOTE 9

NOTES PAYABLE

Notes payable to the Province of Alberta are comprised of the following:

Remaining Term to Maturity	Effective Interest Rate	2006	Effective Interest Rate	2005
Within 1 year	2.57% - 5.54%	\$ 92,843	2.45% - 5.23%	\$ 137,050
1 to 5 years	3.75% - 5.93%	263,492	2.57% - 5.54%	189,374
6 to 10 years	4.26% - 7.64%	192,358	4.28% - 7.64%	274,193
Over 10 years	4.43% - 6.52%	335,395	5.04% - 6.52%	298,898
Accrued interest		<u>12,971</u>		<u>11,138</u>
		<u>\$ 897,059</u>		<u>\$ 910,653</u>

Net unamortized discounts of \$3,347 (2005 \$3,724) are included in the balances disclosed.

Agriculture Financial Services Corporation

NOTE 9

NOTES PAYABLE (CONTINUED)

Principal repayments due in each of the next five years are as follows:

Year ending March 31, 2007	\$	158,704
2008	\$	87,629
2009	\$	159,688
2010	\$	56,088
2011	\$	110,738

The approximate fair value at March 31, 2006 is \$922,702 (2005 \$950,615). Fair values for notes are based on the net present value of future cash flows. Each individual cash flow payment is discounted at a rate which matches the term of the cash flow payment and is adjusted for a yield premium to reflect several factors. They include the following:

- (a) a liquidity premium to reflect that there is a limited pool of these securities for trading in the market, they would be new to the market and are not direct issues of the Province,
- (b) a factor to reflect the blended payment structure of the notes.

NOTE 10

DEFERRED REVENUE

	2006	2005
Government of Canada property and equipment	\$ 8,634	\$ 5,221
Premiums from insured persons	7,730	10,861
Province of Alberta property and equipment	7,503	5,853
	<u>\$ 23,867</u>	<u>\$ 21,935</u>

NOTE 11

REINSURANCE

In addition to the protection provided by reinsurance arrangements between the provincial and federal governments, the Corporation has obtained reinsurance from non-government sources. For crop insurance, the Corporation reinsured a maximum of \$113,652 of the risk from non-government sources. For hail insurance, the Corporation reinsured a maximum of \$6,000 of the risk from non-government sources.

Agriculture Financial Services Corporation

NOTE 12

PENSIONS

The Corporation participates in the multi-employer pension plans, Management Employees Pension Plan and Public Service Pension Plan. The Corporation also participates in the multi-employer Supplementary Retirement Plan for Public Service Managers. The expense for these pension plans is equivalent to the annual contributions of \$2,042 for the year ended March 31, 2006 (2005 \$1,865).

At December 31, 2005, the Management Employees Pension Plan reported a deficiency of \$165,895 (2004 \$268,101) and the Public Service Pension Plan reported a deficiency of \$187,704 (2004 \$450,068). At December 31, 2005, the Supplementary Retirement Plan for Public Service Managers had a surplus of \$10,018 (2004 \$9,404).

NOTE 13

ALLOWANCES FOR DOUBTFUL ACCOUNTS AND FOR LOSSES

	Accounts Receivable (Note 4)	Farm Lending Loans Receivable	Commercial Lending Loans Receivable	Loan Guarantees (Note 14)	Total
Allowances at					
March 31, 2004	\$ 1,104	\$ 31,128	\$ 12,001	\$ 1,263	\$ 45,496
Provision for 2004-05	59	(2,308)	3,921	(77)	1,595
Write-offs in 2004-05, net of recoveries	<u>(34)</u>	<u>(949)</u>	<u>(1,050)</u>	<u>-</u>	<u>(2,033)</u>
Allowances at					
March 31, 2005	1,129	27,871	14,872	1,186	45,058
Provision for 2005-06	280	(1,111)	(1,684)	(362)	(2,877)
Write-offs in 2005-06, net of recoveries	<u>(27)</u>	<u>(495)</u>	<u>(2,025)</u>	<u>-</u>	<u>(2,547)</u>
Allowances at					
March 31, 2006	<u>\$ 1,382</u>	<u>\$ 26,265</u>	<u>\$ 11,163</u>	<u>\$ 824</u>	<u>\$ 39,634</u>

Agriculture Financial Services Corporation

NOTE 14

CONTINGENCIES AND COMMITMENTS

	2006	2005
Loan guarantees	\$ 29,939	\$ 34,716
Less allowances for losses (Note 13)	(824)	(1,186)
	29,115	33,530
Legal actions	887	692
Total contingencies	\$ 30,002	\$ 34,222

The majority of loan guarantees relate to loans made by other financial institutions with repayment guaranteed by the Corporation under the Alberta Farm Development Loans program. The loans outstanding at March 31, 2006 made by other financial institutions were \$47,581 (2005 \$52,788). Loan guarantees under the Alberta Farm Development Loans program include the maximum liability on loan guarantees of \$18,964 (2005 \$23,153) to which the Corporation is exposed under the terms of the agreements with the financial institutions subject to recoveries on underlying securities.

Legal actions represent amounts claimed or amounts claimed in excess of what was accrued. The outcome of the legal actions is not determinable at this time.

The Corporation has a contingent liability in respect of a claim concerning the methodology used to calculate pension benefit payments under Public Service Pension Plan. The claim has been filed jointly and severally against the Province of Alberta and the employers including those participating in the Public Service Pension Plan. The claim specified an amount of \$1,250,000. The Corporation is one out of 587 entities included in the claim and the Corporation's share of liability is not determinable.

	2006	2005
Approved, undisbursed loans	\$ 36,914	\$ 42,861
Reinsurance	15,500	15,615
Estimated farm loan incentives	15,569	14,612
Operating leases	1,003	1,371
Building costs	-	217
Total commitments	\$ 68,986	\$ 74,676

The operating lease commitments are for accommodations with terms up to five years.

Agriculture Financial Services Corporation

NOTE 15

CREDIT RISK AND INTEREST RISK

(a) Credit Risk

Credit risk is the risk that a debtor may not pay amounts owing thus resulting in a loss.

The following table provides a breakdown of the loan receivables by sector. This analysis provides an indication of the concentration of credit risk on the loan portfolio. Significant information is provided throughout these statements to disclose other concentrations of credit risk.

	<u>2006</u>	<u>2005</u>
Loans receivable by sector:		
Grain	\$ 408,360	\$ 410,817
Beef	324,530	320,280
Accommodation and food services	22,935	29,769
Trade - retail and wholesale	32,317	28,438
Hog	25,700	27,860
Manufacturing	29,060	24,713
Processors/Feedmills	4,221	7,767
Other	<u>163,389</u>	<u>170,559</u>
	1,010,512	1,020,203
Allowance	<u>(37,428)</u>	<u>(42,743)</u>
	<u>\$ 973,084</u>	<u>\$ 977,460</u>

(b) Interest Risk

Interest rate risk is the impact future changes of interest rates have on cash flows and fair value of assets and liabilities. The following provides a breakdown of the gaps between the notes payable and the loan portfolio. Because there are no early repayment penalties on most loan programs, the gap analysis includes an adjustment for expected repayments based on historical patterns.

Agriculture Financial Services Corporation

NOTE 15

CREDIT RISK AND INTEREST RISK (CONTINUED)

(b) Interest Risk (Continued)

	Term to Maturity ⁽¹⁾				Not ⁽²⁾ Interest	2006	2005
	Within 1 Year	1 to 5 Years	6 to 10 Years	Over 10 Years	Rate Sensitive	Total	Total
Farm loans	\$ 71,212	\$ 266,913	\$ 235,956	\$ 240,743	\$ (4,492)	\$ 810,332	\$ 812,138
Yield ⁽³⁾	6.85%	6.53%	6.63%	6.25%	-	6.59%	6.87%
Commercial loans	\$ 56,561	\$ 94,032	\$ 12,345	\$ -	\$ (186)	\$ 162,752	\$ 165,322
Yield ⁽³⁾	7.00%	7.11%	5.39%	-	-	6.94%	7.17%
Total	\$ 127,773	\$ 360,945	\$ 248,301	\$ 240,743	\$ (4,678)	\$ 973,084	\$ 977,460
Yield ⁽³⁾	6.87%	6.57%	6.61%	6.25%	-	6.61%	6.89%
Notes payable							
Province of Alberta	\$ 158,704	\$ 414,143	\$ 222,144	\$ 92,444	\$ 9,624	\$ 897,059	\$ 910,653
Yield ⁽³⁾	5.34%	5.35%	5.33%	5.20%	-	5.34%	5.50%
Net gap before prepayment adjustment	\$ (30,931)	\$ (53,198)	\$ 26,157	\$ 148,299	\$ (14,302)	\$ 76,025	\$ 66,807
Estimated prepayment	42,957	72,475	(23,375)	(92,057)	-	-	-
Net gap	<u>\$ 12,026</u>	<u>\$ 19,277</u>	<u>\$ 2,782</u>	<u>\$ 56,242</u>	<u>\$ (14,302)</u>	<u>\$ 76,025</u>	<u>\$ 66,807</u>

The gap positions represent the mismatching of the financing with the loan portfolio at March 31, 2006. The gaps provide an indication of the potential risks to the Corporation if interest rates change. At March 31, 2006 an immediate and sustained increase in interest rates of 1% would increase the net fair market value of loans and financing for the next fiscal year by \$8,129 based on the net gap before prepayment adjustment. A corresponding decrease in interest rates would decrease the net fair market value of loans and financing by a similar amount over the same period.

This gap analysis does not include the investment portfolio, which is disclosed separately below. Investments are not included because investments relate to insurance program cash flows which are managed separately from lending program cash flows.

Agriculture Financial Services Corporation

NOTE 15

CREDIT RISK AND INTEREST RISK (CONTINUED)

(b) Interest Risk (Continued)

The following provides a breakdown of the investment portfolio by term to maturity.

	Term to Maturity ⁽¹⁾				2006	2005
	Within 1 Year	1 to 5 Years	6 to 10 Years	Over 10 Years	Total	Total
Bonds and debentures	\$ 22,487	\$ 116,610	\$ 10,153	\$ 8,038	\$ 157,288	\$ 138,601
Yield ⁽³⁾	3.70%	3.84%	4.65%	5.64%	3.96%	3.98%
Corporate Securities	-	37,451	41,069	-	78,520	31,075
Yield ⁽³⁾	-	4.46%	4.45%	-	4.46%	5.15%
	22,487	154,061	51,222	8,038	235,808	169,676
Accrued interest	180	1,435	936	100	2,651	1,553
	<u>\$ 22,667</u>	<u>\$ 155,496</u>	<u>\$ 52,158</u>	<u>\$ 8,138</u>	<u>\$ 238,459</u>	<u>\$ 171,229</u>

(1) For loans, term to maturity reflects the period of time until an interest rate renegotiation date or the maturity date of the loan. For notes payable, term to maturity reflects the contractual maturity date of the debt. The interest rates are fixed until maturity. Repayment is either by semi-annual, annual installments or full repayment at maturity of principal. For investments, term to maturity classifications are based on contractual maturity date of the security.

(2) Includes general provisions, accrued interest, accrued beginning farmer incentive and unamortized loan discount.

(3) For notes payable and investments, yield represents the rate which discounts future cash receipts to the carrying amount. For loans, yield represents the rate which discounts the stream of future payments from the reporting date to the next interest rate renegotiation date or the rate which discounts future cash receipts to the carrying amount.

Agriculture Financial Services Corporation

NOTE 16

RELATED PARTY TRANSACTIONS

Sufficient information is provided throughout these statements to disclose significant related party transactions the Corporation entered into, except for the following:

	2006	2005
Interest expense - Province of Alberta	\$ 44,849	\$ 45,057
Administration expense - Province of Alberta	1,586	1,864
Administration expense - Government of Canada	374	271

NOTE 17

CROP REINSURANCE FUNDS

The contributions, withdrawals and accumulated deficit positions of the Crop Reinsurance Fund of Alberta and Crop Reinsurance Fund of Alberta for Canada are as follows (see Note 2(f)):

	Crop Reinsurance Fund of Alberta		Crop Reinsurance Fund of Canada for Alberta	
	2006	2005	2006	2005
Opening surplus (deficit)	\$ 2,843	\$ (20,819)	\$ (29,828)	\$ (61,841)
Contributions	11,556	23,662	45,093	32,013
Closing surplus (deficit)	\$ 14,399	\$ 2,843	\$ 15,265	\$ (29,828)

NOTE 18

COMPARATIVE FIGURES

The 2005 figures have been reclassified where necessary to conform to 2006 presentation.

Agriculture Financial Services Corporation

SCHEDULE 1

SCHEDULE OF REVENUE, EXPENSE & SURPLUS

FOR THE YEAR ENDED MARCH 31, 2006

(IN THOUSANDS)

	2006	2005	2006	2005	2006
	Canadian Agricultural Income Stabilization	Canadian Agricultural Income Stabilization	Crop Insurance	Crop Insurance	Lending
Revenue:					
Premiums from insured persons	\$ -	\$ -	\$ 116,968	\$ 115,047	\$ -
Interest	3	3	435	363	68,110
Contribution from Province of Alberta	288,900	202,160	171,628	86,928	8,210
Contribution from Government of Canada	195,710	293,483	95,818	115,307	-
Investment income	1,431	763	10,017	5,957	449
Fees and other income	2,008	2,608	47	62	1,929
Reinsurance recoveries	-	-	-	-	-
	<u>488,052</u>	<u>499,017</u>	<u>394,913</u>	<u>323,664</u>	<u>78,698</u>
Expense:					
Indemnities	472,366	487,887	147,013	156,877	-
Reinsurance	-	-	58,011	44,469	-
Administration, Schedule 2	15,686	11,130	18,454	20,670	22,218
Interest	-	-	39	-	44,849
Adjusting	-	-	6,447	7,206	-
Farm loan incentives	-	-	-	-	4,883
(Recovery) provision for doubtful accounts and for losses (Note 13)	-	-	262	30	(3,157)
Selling commissions	-	-	-	-	-
	<u>488,052</u>	<u>499,017</u>	<u>230,226</u>	<u>229,252</u>	<u>68,793</u>
Surplus (deficit) for the year	-	-	164,687	94,412	9,905
Surplus at beginning of year	-	-	184,976	90,564	61,638
Surplus at end of year	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 349,663</u>	<u>\$ 184,976</u>	<u>\$ 71,543</u>

Agriculture Financial Services Corporation

2005	2006	2005	2006	2005	2006	2005
Lending	Hail Insurance	Hail Insurance	Other	Other	Total	Total
\$ -	\$ 24,556	\$ 20,894	\$ -	\$ -	\$ 141,524	\$ 135,941
70,806	77	57	11	13	68,636	71,242
8,146	-	-	(705)	22,688	468,033	319,922
-	-	-	(610)	22,588	290,918	431,378
310	2,331	2,992	-	-	14,228	10,022
2,192	421	309	370	203	4,775	5,374
-	10	2,163	-	-	10	2,163
81,454	27,395	26,415	(934)	45,492	988,124	976,042
-	21,722	32,281	(2,117)	43,391	638,984	720,436
-	548	420	-	-	58,559	44,889
25,719	1,415	1,323	328	1,177	58,101	60,019
45,057	1	-	138	590	45,027	45,647
-	525	569	674	297	7,646	8,072
5,077	-	-	-	-	4,883	5,077
1,557	18	8	-	-	(2,877)	1,595
-	2,233	2,027	-	-	2,233	2,027
77,410	26,462	36,628	(977)	45,455	812,556	887,762
4,044	933	(10,213)	43	37	175,568	88,280
57,594	39,658	49,871	541	504	286,813	198,533
\$ 61,638	\$ 40,591	\$ 39,658	\$ 584	\$ 541	\$ 462,381	\$ 286,813

Agriculture Financial Services Corporation

SCHEDULE 2

SCHEDULE OF ADMINISTRATION EXPENSE

FOR THE YEAR ENDED MARCH 31, 2006

(IN THOUSANDS)

	<u>2006</u>		<u>2005</u>
	<u>Budget</u>	<u>Actual</u>	<u>Actual</u>
	(Note 3(a))		
Salaries and benefits (Note 12)	\$ 38,019	\$ 33,904	\$ 37,581
Contracted services	7,881	8,765	7,210
Amortization of capital assets	4,700	5,301	4,501
Office accommodation costs	3,222	3,017	3,050
Stationery and supplies	941	1,418	1,645
Data processing	812	1,310	1,165
Travel and automobile	1,088	705	795
Advertising	1,210	699	902
Telecommunications	772	615	724
Postage and freight	604	481	554
Training, meetings, seminars, conferences	596	478	378
Professional services	611	443	613
Directors' fees and expenses	479	413	401
Equipment, rental and maintenance	472	412	360
Miscellaneous	144	140	140
	<u>\$ 61,551</u>	<u>\$ 58,101</u>	<u>\$ 60,019</u>

Agriculture Financial Services Corporation

SCHEDULE 3

SCHEDULE OF SALARIES AND BENEFITS

FOR THE YEAR ENDED MARCH 31, 2006

(IN THOUSANDS)

	2006				2005
	Base Salary ⁽¹⁾	Other Cash Benefits ⁽²⁾	Other Non- cash Benefits ⁽³⁾	Total	Total
Chairman of Board	\$ 72	\$ -	\$ -	\$ 72	\$ 78
Board members ⁽⁴⁾	233	-	-	233	233
President and Managing Director	189	56	36	281	184
Executive/Vice-Presidents					
Vice-President, Finance	149	23	32	204	184
Vice-President, Lending Operations	142	21	31	194	218
Vice-President, Risk Management ⁽⁵⁾	143	33	31	207	49

(1) Base salaries are fees for Chair and Board members and base pay for employees.

(2) Other cash benefits include bonuses and lump sum payments.

(3) Other non-cash benefits include employer's share of all employee benefits, including health care, dental and vision care allowance, group life insurance benefits, pensions, employment insurance, accidental death/dismemberment and long-term disability insurance, workers' compensation and professional memberships. No amount is included in other non-cash benefits for an automobile provided to the President and Managing Director.

(4) The amounts relate to eight Board members during 2005/06 (eight in 2004/05).

(5) This position was created effective January 1, 2005.

Central Offices
 Regional Offices
 District Offices

Fairview Region
 Camrose Region
 Red Deer Region
 Lethbridge Region



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